VZCZCXRO8413
RR RUEHPT
DE RUEHBY #1107/01 3510246
ZNR UUUUU ZZH
R 170246Z DEC 09
FM AMEMBASSY CANBERRA
TO RUEHC/SECSTATE WASHDC 2443
INFO RHEHAAA/WHITE HOUSE WASHINGTON DC
RHMFISS/DEPT OF ENERGY WASHINGTON DC
RUCPDOC/DEPT OF COMMERCE WASHINGTON DC
RUEHOT/AMEMBASSY OTTAWA 0023
RUEHBJ/AMEMBASSY BEIJING 9677
RUEHBN/AMCONSUL MELBOURNE 6849
RUEHPT/AMCONSUL PERTH 5113
RUEHDN/AMCONSUL SYDNEY 5118

UNCLAS SECTION 01 OF 02 CANBERRA 001107

SENSITIVE
SIPDIS

DEPARTMENT FOR EEB/ESC/IEC/ENR/DMONOSSON
DEPARTMENT FOR EAP/ANP

E.O. 12958: N/A
TAGS: EMIN ECON ETRD PGOV AS
SUBJECT: AUSTRALIA'S 3Q GROWTH SLOWER THAN EXPECTED

¶1. (SBU) SUMMARY: Australia's economy slowed to 0.2% GDP growth in the September quarter, despite forecasts of double this result. Treasurer Swan said global conditions are still challenging and the lower-than-expected growth "is a cautionary reminder that growth momentum in the Australian economy is not yet self-sustaining". Most economists had expected the economy to grow by 0.4% in the 3 months to September. The less optimistic result may make the Reserve Bank more cautious about further raising interest rates (ref X). END SUMMARY.

Australian growth continues and broadens

¶2. (SBU). Australia released its National Accounts Data for the September Quarter on December 16, showing economic growth has slowed to a crawl. GDP expanded only 0.2% in the September quarter, compared to stronger growth of 0.6% in the three months to June, and 0.5% in the March quarter. Non-farm GDP grew by 0.3%, while terms of trade rose one per cent and real gross domestic income edged up 0.4%. Second quarter GDP was unrevised at 0.6 per cent, making first-half growth for 2009-10 0.8% and 0.5% over the year to September. Consumer spending advanced 0.7% in the quarter, while exports decreased 2.3% and government spending rose 0.7%. Positive drivers of growth were public gross fixed capital formation (0.3 percentage points), dwellings (0.3) and household final consumption expenditure (0.4). Exports detracted 0.5 percentage points from total expenditure, while imports detracted 1.1 points - the worst trade contribution to GDP since the 1970s.

EXTERNAL ACCOUNTS WORSEN TO FUND RESOURCES INFRASTRUCTURE
--- ----

¶3. (SBU) Foreign trade made its biggest negative quarterly contribution to growth in 35 years due to the impact of lower contract and market prices for coal, iron ore and energy. Exports of goods and services fell 2.3% (seasonally adjusted) in the September quarter, while imports were up by 5.8% - making a 1.6% negative contribution to GDP from this source. Terms of trade have fallen about 16% over the year to September, but there was a 1% lift in the third quarter, suggesting that the worst is now over and commodity prices are beginning to strengthen. Further, rising imports of capital goods should increase export capacity and exports as the global economy recovers. RBA governor Glenn Stevens has argued that a temporarily bigger current account deficit (up 23% in September quarter) caused by increased mining development might be "optimal" if it were financed largely by foreign direct investment.

BUSINESS INVESTMENT PAUSES, BUT INVENTORIES UP
--- -

¶4. (SBU) Private business investment fell in the September quarter, with machinery and equipment down 2.9% and non-residential building investment fell 6.0% (as tax incentives led to a bringing forward of investment to the previous quarter), but the fall would have been larger if not for school investment expansion associated with the Building the Education Revolution program. Commonwealth Bank chief economist Michael Blythe said a slowdown in third quarter growth "was probably unavoidable given the importance of policy supporting growth in the first half of the year". National Australia bank Qgrowth in the first half of the year". National Australia bank chief economist Alan Oster told Econoff that September GDP was lower than expected, due partly to a number of significant revisions by the Australian Bureau of Statistics - such as growth in inventories being revised down from a forecast 1.9% for the September quarter to the actual 0.8% reported in the national accounts. Oster expects a strong December quarter result of around 1% barring major revisions. This is supported by the many strong partial indicators since the end of September, including a 10% pick-up in housing commencements, and Treasury and RBA forecast are still likely to be fairly accurate. (Note: Treasury has forecast GDP will rise 1.5% in the 12 months through June 30, 2010, compared with a May prediction of a 0.5 percent contraction. The RBA forecasts 2.25% growth in 2009-10 year and 3.25 percent in 2010-11).

IMPLICATIONS FOR MONETARY POLICY

¶5. (SBU) The RBA admitted in the minutes of its December meeting (released 15 December) that its decision to raise rates by 0.25 points earlier this month had been a "finely balanced" one. The surprisingly low September GDP result makes a February official interest rate rise much less likely. Assistant RBA governor Ric

Battellino confirmed this on 16 December, when he said "the overall stance of monetary policy is now back in the normal range" so that allowing continued economic recovery may be a priority for the bank at its next meeting in February 2010. The Australian dollar closed lower after these comments, which convinced traders the current cycle of interest rate rises may be nearing its peak. 4Cast Financial Markets economist Michael Turner said debt futures contract prices were reflecting about a 15 per cent chance of a rate rise at the RBA's next meeting, down from about 60 per cent. "It looks like a February rate rise is not going to happen," he said.

GDP REVISIONS MEAN GOA DEBT IS REVISED DOWN

¶6. (SBU) Australia's GDP has been statistically revised so that nominal GDP in 2007-08 is now 4.4% higher, bringing the size of the economy to A$1.25 trillion in 2008-09. Under the new international System of National Accounts (SNA) 2008 standards, the size of government debt has been scaled down. Australia's underlying cash deficit for 2009-10 is now estimated to be 4.5% of GDP and net debt will now peak at 9.6% of GDP in 2013-14, (down from 10% under the previous standard) and will fall to 2.1% in 2019-20 (previously 2.2%).

¶7. (SBU) COMMENT: While Australia's economy is clearly improving, the national accounts show economy is not yet back up to full speed. The fiscal stimulus has provided support but business investment recovery seems fragile - although the end of tax incentives in the previous quarter likely caused the decline in September. Since the third quarter, most partial indicators, such as declining unemployment and increasing housing starts, have been very positive and most economists expect accelerating growth over 2009-10 and beyond.

CLUNE